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Progressive Social Security reform meets reality

Republicans learned some hard political lessons from the failure of their 2005 reform push. Now, it's Democrats' turn.

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From the mid 1990s through the mid 2000s, Social Security reform was a conservative issue. Seemingly every Republican senator or representative had a plan to fix America's underfunded retirement program. Then, after the failure of President George W. Bush's 2005 reform effort, Republican enthusiasm dwindled and Democrats came to have the issue all to themselves.

Now, however, a revised version of the most popular progressive Social Security-reform plan has belatedly recognized a political reality: While ordinary Americans are happy for others to pay more tax dollars into Social Security, they would generally rather not do so themselves.

Before Bush’s failed reform push, conservatives, myself included, were very big on the idea of voluntary personal retirement accounts. The sales pitch was compelling: To fix Social Security’s multi-trillion-dollar funding shortfall, we *could* raise taxes or reduce benefits — but why take those steps when it would be much less painful to raise the rate of return on contributions by investing part or all of a worker’s payroll taxes in personal accounts?

When the rubber met the road, however, it wasn’t that simple. If workers diverted part of their taxes to their own personal accounts, it would leave the program short of the funds needed to pay for current retirees’ benefits. Even if personal accounts added to retirees’ incomes, the traditional benefits paid by Social Security would still have to be reduced to make the program solvent. And finally, financial markets pay a higher rate of return not as a freebie, but as a reward for investors’ taking on greater risk. Thus, what initially seemed like a free lunch turned out not to be, and selling the idea to senators and representatives was ultimately much harder than placing op-eds in newspapers. Despite an all-out push by President Bush and Republican control of both houses of Congress, Social Security reform ran out of steam. The idea of personal accounts polled well, and even continued to do so well after Republican enthusiasm for it had waned. But passing reform legislation turned out to be much more politically difficult than conservatives had hoped.

Now, it’s Democrats’ turn to learn the same lessons. For around a decade, a small group of progressive activists has argued that the real problem with Social Security isn’t its funding so much as its lack of generosity, and its argument has won the day with Democratic lawmakers. Nearly every Democratic member of the House of Representatives has formally endorsed the Social Security 2100 Act, which was first introduced by Representative John Larson (D., Conn.) in 2013. The proposal has gone through various iterations since then, all of which would increase benefits for rich and poor alike by raising taxes on rich and poor alike. Larson had hoped that, after Democrats gained control of Congress and the presidency at the end of 2020, historic Social Security reform could come in 2021.

But, as Republicans found out when Social Security reform moved from a policy issue to a presidential-agenda item under Bush, getting across the finish line is the hardest part.

Changes to the 2021 version of the Social Security 2100 Act, released on October 26, acknowledge that difficulty. But in doing so, they also clarify the true choice Americans face: If they want higher Social Security benefits, they’ll have to pay for those benefits themselves — and they may choose differently than progressive lawmakers prefer.

Previous versions of Larson’s proposal included two types of tax increases.

First, the 12.4 percent Social Security payroll tax, which currently applies to yearly earnings up to $147,000, would be applied to yearly earnings up to $400,000. Because the current law's payroll-tax ceiling is indexed to wage growth while the new $400,000 threshold would be unindexed, this "donut hole" would shrink each year until eventually, all workers would pay the Social Security tax on all of their wages. This would immediately increase the effective top marginal tax rate on earned income by twelve percentage points, giving the U.S. one of the highest such rates in the world.

Prior versions of Larson's plan also gradually increased the Social Security-payroll-tax rate, from the current 12.4 percent up to 14.8 percent over the next two decades, so every worker, regardless of his salary, would pay more. In return for higher taxes, Americans would receive two things: a Social Security program that was solvent for 75 years or more, and increased Social Security benefits.

Under the 2021 version of the plan, however, Americans would receive neither of those things. In a belated acknowledgment of political reality, the plan eliminates the payroll-tax-rate increase that would have hit low- and middle-income workers. This in turn has dramatic knock-on effects. The payroll-tax-rate increase supplied nearly half of the additional revenues in previous iterations of the plan. Without it, the 2021 version would only be able to add four years, rather than 75, to the life of the Social Security trust funds, and instead of being permanent, the benefit increases that Larson has long promised Americans would last only five years and then be repealed in full.

While marrying temporary solvency to temporary benefit increases is an obvious gimmick designed to leverage further tax increases down the road, it also presents ordinary Americans with a clear choice: If they want higher Social Security benefits, they're going to have to pay for those benefits themselves. Larson's proposal already hits high earners harder than our political system is likely to accept. In fact, almost no developed countries fund their pension systems with an uncapped payroll tax.

But even if they proved politically feasible, the increased Social Security taxes essential to progressives' reform schemes aren't likely to be popular with voters. Americans already have greater faith in their personal savings than in Social Security. A 2015 opinion survey published by the Investment Company Institute found that 81 percent of Americans were somewhat or very confident that an IRA or 401(k) account could help them attain retirement security. On the other hand, only 35 percent of Americans in a 2016 survey conducted by the Employee Benefit Research Institute said that they were somewhat or very confident that Social Security would pay them benefits at least equal to what today's retirees receive.

A more recent public-opinion survey confirmed Americans' preferences. Last year, I commissioned a question in the RAND Corporation's American Life Panel: "Some Americans are concerned about not having enough income once they retire. If you wished to increase your future retirement income, would you prefer to: Pay higher Social Security taxes while working and receive a higher Social Security benefit you prefer to: Pay higher Social Security taxes while working and receive a higher Social Security benefit when you retire? Or make higher contributions to a private retirement account such as an IRA or 401(k) and receive higher income from that account when you retire?" No matter their gender, race, education level, yearly income, or state of residence, strong majorities of Americans responded that they would rather boost their retirement incomes through personal savings than through expanding Social Security. Overall, 74 percent of Americans preferred increasing their personal savings while just 26 percent favored paying more into Social Security.

None of this is to say that Americans would react to a Democratic drive to enact the Social Security 2100 Act by embracing benefit reductions over tax increases. As they did in 2005, Americans could simply choose to kick the can down the road and hope that future generations will pick up the tab. But nearly two decades after President Bush's failed Social Security reform efforts, the amount of time that we can continue to procrastinate has diminished considerably.

One lesson from President Bush's failure to pass Social Security reform, as well as President Obama's skin-of-his-teeth passage of the Affordable Care Act despite overwhelming Democratic House and Senate majorities, is that it is much easier to play defense on entitlement reform than to play offense. Republicans can likely defeat a Democratic Social Security-reform plan today as easily as Democrats defeated the 2005 Republican plan. Voters don't generally require a party that opposes entitlement reforms to put forward its own plan; they will reward it merely for opposing the difficult choices inherent in the other side's plan.

The ultimate solution to this problem has to be genuinely bipartisan Social Security reform. Progressives won't like that, and I won't like it either — we both want reform to be done *our way*. But if lawmakers want Social Security fixed and recognize the difficulty of doing anything large on a purely partisan basis, they need to be willing to split the difference. That could mean increasing benefits for low-income retirees, something that policymakers in both parties have suggested in the past. It could mean some increases in the maximum salary subject to Social Security taxes, targeted benefit reductions, a higher retirement age, or tweaks to the formula used to calculate cost-of-living adjustments. It could also mean enacting universal retirement-savings accounts, either through Social Security or employer-sponsored 401(k) plans.

None of this would be perfect public policy from anyone's partisan perspective. But when is the last time we got that?